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January 4, 1995

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VIA FEDERAL EXPRESS

Mr. William F. Caton

Acting Secretary

Federal Communications Commission

1919 M Street, NW, Room 222

Washington, D.C. 20554

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JAN 05 1995

FEDERAL ROOM

Re: Supplemental Comments of the Small Cable Business Association and Letter from Small Cable Business Association Chairman David Kinley to Chairman Reed Hundt; MM Docket Nos. 92-266 and 93-215

Dear Mr. Caton:

Enclosed for filing in MM Docket Nos. 92-266 and 93-215 are the above-referenced documents. We have enclosed the original and nine copies for distribution. We are also enclosing one copy that we ask that you return to us in the enclosed envelope after it has been file stamped "Received".

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Mr. William F. Caton

January 4, 1995

Page 2

If you have any questions or need additional information, please contact us.

Very truly yours,

HOWARD & HOWARD

A handwritten signature in black ink, appearing to read "Eric E. Breisach", with a long horizontal flourish extending to the right.

Eric E. Breisach

EEB:mtd

Enclosures

**cc: Chairman Reed Hundt
Commissioner James H. Quello
Commissioner Andrew C. Barrett
Commissioner Rachelle B. Chong
Commissioner Susan Ness
Meredith Jones
Blair Levin**

EX PARTE OR LATE FILED

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)

Implementation of Sections of)
The Cable Television Consumer)
Protection and Competition Act)
of 1992)

Rate Regulation)

MM Docket No. 92-266

MM Docket No. 93-215 **FILED**

JAN 05 1995

**SUPPLEMENTAL COMMENTS
OF
THE SMALL CABLE BUSINESS ASSOCIATION**

FCC MAIL ROOM

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Dated: January 4, 1995

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I. SUMMARY

The Cable Telecommunications Association ("CATA") has approached the Commission with an plan for alternate rate regulation of systems with 1,000 or fewer subscribers. The Small Cable Business Association ("SCBA") fully supports the CATA proposal as far as it goes and urges the Commission to adopt it immediately.

The Commission must be cognizant, however, that even after granting this relief, significant "small" operator and company issues will remain and must be resolved. SCBA has been active in both benchmark and cost-of-service rulemaking dockets, documenting and proposing relief for small companies and small systems. SCBA will continue to pursue these issues until meaningful relief is forthcoming.

The CATA proposal is important because it gives local franchise authorities the flexibility to take local factors, including higher costs, into account, without requiring completion of time consuming cost-of-service calculations. SCBA has always supported such local flexibility as evidenced by its proposed modifications to the rate freeze. SCBA remains concerned, however, that some operators will not be able to avail themselves of this relief given that the franchise authority must be willing to venture down the alternate regulation path. Where franchise authorities are unwilling or politically unable to use alternate regulation, the need for fundamental changes in the amount of effort needed to regulate rates and the amount of the rates that may be charged remains evident.

Therefore, even if the Commission adopts the CATA proposal, which SCBA strongly urges the Commission to do, it must still address the following issues:

- Small companies need benchmark adjustments to offset higher costs of programming and lower amounts of unregulated revenue;

- Small companies need lessened regulatory burdens;
- Small systems need benchmark adjustments to recover headend costs and high per subscriber capital costs when adding channels;
- Small systems need to include those with more than 1,000 subscribers;
- Low density systems need benchmark adjustments to recover higher per subscriber capital and operating costs; and
- Small companies need different interim cost-of-service presumptions to provide an adequate safety net.

Each of the foregoing have been raised on the record by SCBA. Moreover, each has been documented and specific adjustments or changes to the regulations proposed by SCBA. To date, the Commission has yet to act on many of these issues. While SCBA urges the Commission to grant the CATA proposal, that action, in and of itself, will not lessen the need or the urgency to address the needs listed above.

II. INTRODUCTION

These *Supplemental Comments* are filed in response to a request by the Chief of the Cable Services Bureau for the input of the Small Cable Business Association ("SCBA") regarding a proposal¹ by the Cable Telecommunications Association ("CATA") to lessen the administrative burdens on systems with 1,000 or fewer subscribers. Given that any proposal dealing with small system regulation impacts many of SCBA's members, in whole or in part, SCBA is keenly interested in such proposals.

SCBA is a self-help group formed by small cable operators faced with an unprecedented labyrinth of overwhelming regulation. SCBA's primary purpose is to help small operators learn, understand and implement the new requirements.

SCBA is only in its second year of existence. It began when several small operators decided to meet in Kansas City on Saturday May 15, 1993. Word of the meeting spread and one hundred operators attended. The Small Cable Business Association was formed by the end of the day.

From its simple beginnings, SCBA has rapidly grown to over 340 members. More than half of them have fewer than 1,00 subscribers in total. SCBA continues its mission to educate and assist small operators using unpaid volunteer leadership. Despite its limited resources, SCBA has been very active in the rulemaking process in this Docket and has always provided input and information when requested by Commission personnel.

¹The proposal was first contained in a letter to Chairman Reed Hundt from Stephen Effros dated September 23, 1994 and supplemented in a letter dated October 17, 1994 to Meredith Jones, Chief, Cable Services Bureau. Both of these letters were filed in Docket 92-266 on September 26, 1994.

III. SCBA SUPPORTS THE CATA PLAN FOR SMALL SYSTEM RELIEF

A. Summary Of CATA Proposal

CATA proposes that the Commission amend its regulations to permit an "informal" alternate rate regulatory process for systems with 1,000 or fewer subscribers. This "informal" process would allow certified franchise authorities and cable operators to determine mutually agreeable rate levels outside of the current benchmark/full reduction or cost-of-service methodologies. Such rate determinations could cover both basic and cable programming services tiers ("CPST"), with the Commission retaining sole jurisdiction over the CPST but giving weight to local findings. The cable operator may opt out of alternative regulation should the outcome be unfavorable.

B. SCBA Supports The CATA Proposal

In many ways, the CATA proposal for alternative regulation mirrors in concept SCBA's plan for rate freeze relief outlined in its December 9, 1993 *Emergency Petition*². In the *Emergency Petition* SCBA advocated that systems with 1,000 or fewer subscribers could raise rates during the rate freeze period where the cable operator's rates after the increase remained at or below the benchmark rate and the franchise authority consented to the basic tier rate increase. SCBA outlined significant public policy reasons for allowing very limited local waivers of the rate freeze³. Despite the factors outlined in the *Emergency*

²*Emergency Petition for Interim Procedures and Limited Reconsideration of Rate Freeze Order*, Small Cable Business Association, MM Docket 92-266 (Dated December 9, 1993).

³The United States Small Business Administration, Office of Chief Counsel for Advocacy, in a letter dated January 27, 1994 to Chairman Reed Hundt "strongly urge[d] the Commission to grant the SCBA's petition while it consider[ed] more comprehensive solutions to the disparate impact of rate regulation on small cable operators." The United

Petition and after follow-ups with the Commission, including a letter to Chairman Hundt dated February 18, 1994⁴ in which SCBA described a small operator who was reducing services because the rate freeze prevented an increase in rates that was approved by the franchising authority following public hearings. In that case, the franchise authority requested that the operator rebuild its system and add new services. In return, the franchise authority approved rate increases; increases that were later prohibited by the rate freeze.

Creating flexibility at the local level is very important to the regulation of small systems and operators. This flexibility is at the hub of CATA's proposal. SCBA fully supports the CATA proposal but not as the sole action for small system and operator relief by the Commission.

States Small Business Administration stated that the proposal "strikes the appropriate balance between consumer protection and the financial health of small cable operators." Despite this and other support, the Commission never acted on SCBA's *Emergency Petition*. SCBA urges the Commission not to disregard CATA's proposal in the same manner.

⁴Letter from SCBA Counsel Eric Breisach of Howard & Howard to Chairman Hundt.

IV. UNRESOLVED SMALL SYSTEM AND SMALL OPERATOR PROBLEMS REMAIN EVEN IF THE CATA PLAN IS ADOPTED

Even though alternate regulation will provide relief in certain circumstances, it heavily relies on franchising authorities to "do the right thing." It has been the experience of many SCBA members that often political forces are at play within franchising authorities that prohibit this. Particularly where vocal minorities exist, it is very difficult for publicly elected officials to take actions that do not result in lower subscriber rates. Consequently, SCBA is concerned that more often than not, operators of small systems will find that franchise authorities will not be able to avail themselves of the alternate regulatory structure. Nevertheless, these operators remain in dire need of relief from both the administrative burden of rate relief and the ability to charge rates that will allow them to continue providing services.

Small operators and operators of small systems with more than 1,000 subscribers who face unique problems imposed by the disparate impact of rate regulation on them remain without relief. Their needs, needs that have been repeatedly articulated by SCBA in its filings and meetings with the Commission, are not addressed by the proposed alternate regulatory method.

Even if the Commission grants the alternate regulatory method, many concerns will remain and must be dealt with by the Commission. To assist the Commission in its review of this matter, we outline below many of these pressing problems as well as solutions and information that SCBA has entered into the record of the various rate regulation dockets.

A. Small Companies Need Relief

1. Description. SCBA has repeatedly stated that small companies, not only small systems, are disparately impacted by rate regulation. From an administrative side, small operators do not have the corporate resources to cope with rate regulation. Small companies typically lack economies of scale and typically serve areas with higher operating costs.
2. SCBA Proposed Solution. SCBA has proposed adoption of a meaningful small company size definition. The current 15,000 subscriber definition is wholly inadequate⁵. SCBA has proposed a series of additions to the benchmarks⁶, many of which addressed the cost of operating a small cable business, including the following:
 - a. Cost of Programming - A benchmark adjustment based on company size should be allowed given that SCBA members and

⁵The size definition is currently the subject matter of a *Petition For Review* in the matter of *Time Warner Entertainment Co., L.P. v. Federal Communications Commission*, No. 93-1723 (D.C. Cir). Also, in response to the *Fifth Notice of Proposed Rulemaking*, SCBA and others submitted comments justifying enlargement of the small company standard to a company receiving less than \$40 - \$100 million in gross annual receipts. (See, *Comments of the Small Cable Business Association* in MM Docket 92-266, dated November 15, 1994).

⁶Although the adjustment computations were performed prior to the *Second Order on Reconsideration* in which a new competitive differential was factored into the benchmark equation, the adjustments are based on the underlying benchmark sample attributes and therefore are unaffected by the new differential. They remain valid.

other smaller companies pay 54 percent more for programming than larger MSOs that comprised the database from which the benchmark formula was derived. Complete details were provided and a benchmark adjustment was computed in the February 15, 1994 *SCBA Benchmark Adjustment* filing⁷. The Commission did not address this issue in any rulemaking.

- b. **Absence of Additional Unregulated Revenue** - Small companies typically are unable to offer the same array of unregulated services that larger companies offer. An analysis of the systems used to derive the benchmark formula reveals that those systems not affiliated with a top-25 MSO have two fewer pay services. This means that, on average, smaller companies have a minimum of \$2.60 smaller margin to pay operating costs than do larger operators⁸. The Commission did not address this issue in any rulemaking.

- c. **Lessened Regulatory Burden** - Small companies do not have the

⁷*Supplemental Comments in Further Support of Interim Benchmark Adjustments for Low Density and Smaller Cable Operators*, Small Cable Business Association, MM Docket No. 92-266 (Filed February 15, 1994) ("*SCBA Benchmark Adjustments*").

⁸See *SCBA Benchmark Adjustments* at p. 10 and *Supplemental Comments and Plan for Interim Relief for Low Density and Smaller Cable Businesses*, Small Cable Business Association, MM Docket No. 92-266 (Filed January 31, 1994), at pp. 9-10.

internal staffs to cope with the tremendous burden of rate regulation. By the Commission's own disclosures to the Office of Management and Budget, it takes an operator at least 40 hours to prepare a benchmark filing and 120 hours to prepare a cost-of-service filing⁹. These totals are per franchise area. This means that if an operator has 17 franchise areas, it will need to hire a full time person just to fill out rate regulation forms! SCBA still advocates industry wide cost averaging for equipment basket computations¹⁰. SCBA as suggested or supported other streamlining plans including comparison of rates to 1986 levels, streamlined cost-of-service showings and net income showings¹¹. Several of these options have never been discussed in any rulemaking.

B. Small Systems Need Relief

1. **Description** - Operators of smaller systems have higher per subscriber costs than larger systems. This occurs because many costs an operator has are fixed and when spread among a smaller group of subscribers

⁹*Comments* by the Small Cable Business Association with respect to establishing a new company size standard, MM Docket 92-266 dated (November 15, 1994).

¹⁰*Combined Comments and Reply Comments*, Small Cable Business Association, MM Docket No. 93-215 (dated August 30, 1993) at pp. 12-13.

¹¹*Reply Comments*, Small Cable Business Association, MM Docket No. 93-215 (September 13, 1994), pp. 31 - 34.

result in a high per subscriber cost.

2. SCBA Proposed Solution - SCBA has compared the costs incurred by smaller systems to those of the profile used to develop the benchmark formula. Based on this comparison, SCBA has computed specific benchmark adjustments based on system size. Specific items needing adjustment are listed below:

- a. Headend Costs - A prime example of such costs are headend costs¹². SCBA has proposed an average headend cost adjustment¹³. As noted in its earlier filings, the specific adjustment is understated for many operators given that certain rural operators or operators in difficult terrain typically spend greater amounts on headend equipment to receive local off-air signals.
- b. Channel Expansion - Small system operators, as the Commission recently pointed out, incur higher per subscriber

¹²In fact, the Commission has itself recognized this higher cost born by smaller systems in the *Sixth Order on Reconsideration* when, as part of its going forward rules, it allowed the cost recovery of headend costs for smaller systems but only as an alternative to the per-channel add-on.

¹³SCBA *Benchmark Adjustments* at p. 7.

capital costs than larger systems. SCBA has proposed a higher cost recovery add-on for smaller systems¹⁴. Although the Commission has recognized this issue, it has not crafted an effective mechanism to alleviate the problem¹⁵.

C. The Definition Of Small Systems Needs To Be Enlarged

1. Description - The definition of a small system as applied by the Commission is underinclusive. Systems with 1,001 subscribers face virtually identical problems as those with 1,000 subscribers.
2. SCBA Solution - A bright line cannot be drawn between large and small systems. Rather, relief should be provided on a sliding scale, with smaller systems receiving greater relief. The Congressional mandate did not specify how system size was to be measured (i.e. total subscribers or by individual franchise areas). It also did not preclude relief for systems with more than 1,000 subscribers that are still "small". Relief should be provided on a sliding scale basis with self-limiting adjustments (i.e., as system size grows, the adjustment eventually becomes zero).

¹⁴SCBA *Benchmark Adjustment* at pp. 7-8.

¹⁵The Commission has made the going forward headend cost recovery adjustment an alternative to the \$0.20 per channel addition, rather than allow the headend cost adjustment as an additional recovery. This, in effect, negates the relief.

D. Low Density Systems Need Relief

1. Description - Cable systems with fewer homes and subscribers per mile have higher capital and operating costs per subscriber. This results from capital investment for each mile of cable plant regardless of population density. Often accompanying low population densities are higher operating costs (i.e., the mere dispersion of customers requires higher costs to travel to customer locations to perform installation and service work).
2. SCBA Proposed Solution - SCBA has documented the capital and operating costs of low density operators and compared them to the benchmark sample. The resulting differentials have been set out in tables in the *SCBA Benchmark Adjustments*, pp. 5 - 7 and Table B. The Commission has not only failed to act on these proposals, in the recent *Second Order on Reconsideration*, it allowed operators with more than 15,000 subscribers to seek classification as a "small operator" based on a showing of higher operating costs¹⁶ and therefore attempt to avoid further rollbacks¹⁷. The Commission has missed the mark.

¹⁶*Second Order on Reconsideration* at fn. 161.

¹⁷The Commission has not been specific regarding how operators are to demonstrate that they have "higher costs" than some other group of operators when the Commission has not accumulated any cost information and has disregarded cost differential information that SCBA has made part of the record.

Instead of avoiding further rate rollbacks (i.e., the additional 7 percent) low density operators should not have been required to take any rate rollbacks.

E. Small Systems and Small Companies Need Cost-Of-Service Relief

1. Description - The Commission has held out the cost-of-service alternative as the safety net to protect higher cost systems from inappropriate rate reductions under the benchmark/full reduction methodology. Nevertheless, the two rate computation methodologies lack parity for small systems and small operators. The benchmark/full reduction methodologies include a number of special considerations for small systems and operators. No similar provisions exist in the cost-of-service rules; rules which often have a harsher impact on small systems and companies¹⁸.
2. SCBA Proposed Solution - SCBA has requested that the Commission, in addition to addressing this disparity in its final cost-of-service rules, immediately adopt a separate set of interim cost-of-service

¹⁸For example, the limitation of the recovery of prior year losses to the FAS 51 standard, while wholly inappropriate in all events, is harsher on small systems given that by definition, they typically have a shorter or non-existent FAS 51 period. SCBA has more fully described this and other disparities in its *Comments* in MM Docket 93-215, filed July 29, 1994.

presumptions for small operators and small systems¹⁹. Only with such different presumptions will cost-of-service showings create an adequate safety net for small operators and systems.

¹⁹Again, the definitions of small operators and small systems need to be expanded.

V. SUMMARY

The CATA proposal helps alleviate some concerns faced by some operators. SCBA strongly urges the Commission to adopt this relief. Nevertheless, since the alternate mechanism may be used at the discretion of the franchise authority, some operators will not be able to avail themselves of the relief. These operators still need to be afforded various forms of relief that SCBA has set forth before the Commission in filings over the past 17 months, the highlights of which are outlined above.

Respectfully submitted,

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